

Message Text

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TO SECSTATE WASHDC IMMEDIATE 9850

C O N F I D E N T I A L LIMA 3787

LIMDIS

E.O. 11652: GDS

TAGS: EFIN PE

SUBJ: PERU'S FINANCIAL CRISIS

REF: STATE 107845

SUMMARY: PRESIDENT MORALES BERMUDEZ TOLD ME THAT THE PACKAGE OF ECONOMIC AND FISCAL MEASURES DESIGNED TO PROVIDE THE BASIS FOR A NEW AGREEMENT WITH THE IMF IS NOW SET BUT WILL NOT BE ANNOUNCED UNTIL SHORTLY AFTER THE ELECTION. HE ARGUED THAT ANNOUNCEMENT BEFORE JUNE 4 WOULD JEOPARDIZE THE ELECTION. THE PRESIDENT HOPES THAT THE PRIVATE BANKS WILL PROVIDE SOME BRIDGE FINANCING IN THE INTERIM IF THEY CAN BE PERSUADED TO DROP THEIR INSISTENCE ON PRIOR IMPLEMENTATION OF THE PACKAGE, AND IF THE IMF GIVES THE GREEN LIGHT. MORALES BERMUDEZ ASKED FOR OUR SUPPORT. END SUMMARY.

1. I DELIVERED PRESIDENT CARTER'S LETTER TO PRESIDENT MORALES BERMUDEZ TODAY AT NOON. WE SPENT ABOUT FORTY MINUTES DISCUSSING PERU'S FINANCIAL PROBLEMS AND THE FOREIGN MINISTER'S UPCOMING TRIP. MORALES BERMUDEZ READ THE LETTER IN MY PRESENCE. IT APPEARED TO OFFER HIM NO SURPRISES. (COMMENT: I AM DISAPPOINTED, TO SAY THE CONFIDENTIAL

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LEAST, THAT THE DESK SAW FIT TO MAKE THE LETTER AVAIL-
ABLE TO THE PERUVIAN EMBASSY IN WASHINGTON PRIOR TO MY
MEETING WITH THE PRESIDENT.) HE SAID NOTHING ABOUT THE
NEGATIVE ON THE ESF LOAN BUT COMMENTED THAT PRESIDENT
CARTER'S REFERENCE TO RESCHEDULING PERU'S DEBT WAS MOST
IMPORTANT. THE EFFORTS SO FAR TO RESOLVE PERU'S BOP
PROBLEM IN HIS VIEW HAVE BEEN NO MORE THAN "PALLIATIVES".

ONLY A "RESTRUCTURING" OF THE DEBT WILL ALLOW PERU TO GO FORWARD ECONOMICALLY.

2. MORALES BERMUDEZ SAID THAT THE GOP NEEDS OUR "POLITICAL SUPPORT" FOR THAT PURPOSE. BUT, HE ADDED, USG SUPPORT IS REQUIRED IN ADVANCE OF SUCH AN OPERATION TO HELP PERU GET OVER THE NEXT CRITICAL WEEKS. HE DESCRIBED THE SCENARIO AS FOLLOWS: THE FOREIGN MINISTER WILL GO TO WASHINGTON TOMORROW TO PRESENT PERU'S "POLITICAL" CASE. FINANCE MINISTER SAENZ, ASSUMING HE RECOVERS FROM THE ILLNESS THAT STRUCK HIM IN MEXICO, WILL FOLLOW NEXT WEEK TO NEGOTIATE AN AGREEMENT IN PRINCIPLE WITH THE FUND AND TO ATTEMPT TO OBTAIN BRIDGE FINANCING FROM THE BANKS. RENEGOTIATION OF THE DEBT WILL BE THE THIRD AND FINAL STEP.

3. THE PRESIDENT SAID THAT THE PACKAGE OF ECONOMIC AND FISCAL MEASURES HAS NOW BEEN APPROVED, THE DECREES PREPARED AND SIGNED. THE PACKAGE HAS BEEN PRESENTED TO THE FUND AND IS CURRENTLY BEING REVIEWED AT THE STAFF LEVEL. HOWEVER, THE PRESIDENT AND THE JUNTA DECIDED YESTERDAY THAT THE MEASURES WOULD NOT BE ANNOUNCED OR GO INTO EFFECT UNTIL A FEW DAYS AFTER THE JUNE 4 ELECTIONS. MORALES BERMUDEZ WITH CONSIDERABLE VIGOR ARGUED THAT THESE "VERY HARD" DECREES WOULD THREATEN THE POLITICAL PROCESS IF PUBLISHED NOW. HE SAID IT MIGHT WELL BE CONFIDENTIAL

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NECESSARY TO IMPOSE EMERGENCY MEASURES, USE THE TROOPS AND IN GENERAL EMPLOY REPRESSION IF THE ANNOUNCEMENT WERE TO BE MADE IN THE HEAT OF THE POLITICAL CAMPAIGN. THE POLITICAL PARTIES, WHICH ARE ALL RUNNING AGAINST THE GOVERNMENT, WOULD QUITE NATURALLY PLAY TO POPULAR PASSIONS. ON THE OTHER HAND, MORALES BERMUDEZ THOUGHT THAT THE MEASURES CAN BE PUT ACROSS WITHOUT UNDUE DIFFICULTY IN THE WAKE OF THE ELECTIONS.

4. HE EXPRESSED HIS UNDERSTANDING OF THE POSITION TAKEN BY THE BANKS TO THE EFFECT THAT ANNOUNCEMENT AND IMPLEMENTATION OF THE PACKAGE MUST PRECEDE ANY NEW FINANCING. BUT HE HOPED THIS POSITION COULD BE CHANGED IF THE IMF INDICATES ACCEPTANCE OF THE PACKAGE AND IF WE OFFER OUR SUPPORT.

5. I ASKED THE PRESIDENT IF THE COUNTRY COULD GET THROUGH THESE NEXT WEEKS IN THE EVENT THE BANKS DID NOT PROVE FORTHCOMING. HE SAID THAT THE CENTRAL BANK COULD PROBABLY CONTINUE TO SERVICE OFFICIAL DEBT BUT ONLY AT THE EXPENSE OF THE PRIVATE SECTOR. HE FORESAW MOST SERIOUS CONSEQUENCES FOR THE PRIVATE SECTOR IF SOME

RELIEF IS NOT PROVIDED SOON. I RESPONDED BY POINTING OUT PRESIDENT CARTER'S STATEMENT THAT ANY AGREEMENT WITH THE FUND MUST BE WORKED OUT DIRECTLY, EMPHASIZING THAT WE COULD NOT INTERFERE IN WHAT HAS TO BE A TECHNICAL PROCESS. I ALSO EXPRESSED SOME PESSIMISM ABOUT THE RESPONSIVENESS OF THE BANKS BUT INDICATED THAT WE WOULD BE LOOKING INTO THAT SITUATION. AS FOR THE POSTPONEMENT OF THE PACKAGE, I SAID THAT WAS A POLITICAL DECISION THAT ONLY THE GOVERNMENT OF PERU COULD MAKE. MORALES BERMUDEZ INSISTED THAT THE MEASURES WOULD BE TAKEN AS SOON AS POSSIBLE, COMMENTING THAT THE GOP IS IN DIRE NEED OF THE FISCAL RESOURCES THESE WILL PROVIDE.

6. THE PRESIDENT ASKED AGAIN FOR OUR SUPPORT. HE
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SAID HE KNEW THAT THE POLITICAL TRANSITION HIS GOVERNMENT IS MAKING EVERY EFFORT TO CARRY OUT IS IMPORTANT TO OUR LATIN AMERICAN POLICY. HE SAID HE WAS DETERMINED TO COMPLETE THE POLITICAL CALENDAR ON SCHEDULE AND TO TRANSFER POWER AS HE HAS PROMISED. I SAID WE WOULD BE EXPLORING WITH THE FOREIGN MINISTER IN WASHINGTON THE QUESTIONS HE RAISED AND WOULD DO OUR BEST TO BE HELPFUL. I SUGGESTED THAT DE LA PUENTE BE PREPARED TO LAY OUT IN DETAIL FOR OUR PEOPLE THE AGREED-UPON PACKAGE. MORALES BERMUDEZ SAID HE WOULD BE.

7. COMMENT: IT HAS BEEN CLEAR FOR SOME TIME THAT THE ELECTIONS COME FIRST AS FAR AS THE PRESIDENT IS CONCERNED, AND THAT THE DELAY IN TACKLING THE FINANCIAL CRISIS HAS BEEN DUE IN PART TO THAT PRIORITY. IT IS TRUE THAT THE GOP COULD HAVE MOVED SIX WEEKS AGO WITHOUT SO MUCH RISK TO THE ELECTORAL PROCESS. BUT THAT WATER IS NOW OVER THE DAM.

8. DESPITE THE CONFUSION AND IRRESOLUTION THE GOP PERSISTS IN DEMONSTRATING, WE CONTINUE TO BELIEVE THE PRESIDENT'S EFFORTS DESERVE OUR SUPPORT. (FOR ONE THING, THE ELECTIONS AND THE INCREASINGLY PROBABLE SUBSEQUENT INTRODUCTION OF CIVILIANS INTO THE KEY FINANCIAL POSTS LOOK TO BE ABOUT THE ONLY MEANS OF BRINGING SOME DEGREE OF DECISIVENESS AND RATIONALITY TO THE GOP'S ATTEMPTS TO COPE WITH THE FINANCIAL CRISIS.) HOW WE CAN EFFECTIVELY SHOW THAT SUPPORT IS NOT CLEAR. A TOKEN ESF PARTICIPATION IN A FINANCIAL BRIDGING EXERCISE WOULD HAVE HAD THE MOST IMPACT. PERHAPS SOME KIND OF ANNOUNCEMENT ON THE DEBT-RENEGOTIATION FRONT MIGHT BE WORKED OUT, AS I HAVE PREVIOUSLY SUGGESTED.
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